Declassified in Part - [redacted]
Sanitized Copy Approved for [redacted]
Release 2011/10/31 : [redacted]
CIA-RDP85T00875R00160003
[redacted]

~~Secret~~

[redacted] 25X1

DIRECTORATE OF INTELLIGENCE

Intelligence Memorandum

Sudan: Economic Implications Of Growing Pan Arabism

25X1

~~Secret~~

ER IM 70-93
July 1970

Copy No. 49

Declassified in Part - Sanitized Copy Approved for Release 2011/10/31 : CIA-RDP85T00875R001600030093-6

WARNING

This document contains information affecting the national defense of the United States, within the meaning of Title 18, sections 793 and 794, of the US Code, as amended. Its transmission or revelation of its contents to or receipt by an unauthorized person is prohibited by law.

GROUP 1
Excluded from automatic downgrading and declassification

Declassified in Part - Sanitized Copy Approved for Release 2011/10/31 : CIA-RDP85T00875R001600030093-6

CENTRAL INTELLIGENCE AGENCY
Directorate of Intelligence
July 1970

INTELLIGENCE MEMORANDUM

Sudan: Economic Implications Of Growing Pan Arabism

Introduction

Sudan's second year under a military government, established by a coup in May 1969, promises to be one of increasing orientation toward the radical Arab and Communist worlds. Personal freedom already is greatly circumscribed, and socialization of the economy is progressing rapidly. Communist aid is replacing Western aid. Serious economic problems, the result of excessive domestic bank financing of ambitious development plans, weak and graft-ridden governments, and internal dissension, were inherited from the preceding government. Strong measures have been introduced to curb inflation, reduce imports, and improve the country's finances. This memorandum examines the conditions leading to Sudan's present position of near bankruptcy and the major policies adopted by the post-coup government to meet the long-standing economic crisis.

Background

1. Sudan, Africa's largest country, is in some respects two nations in one. The northern two-thirds, containing the country's major cities, the seat of government, and most of modern economic activity, is inhabited primarily by Arab Muslims whose historic and religious ties are to the Arab states to the north. The three southern provinces are inhabited

Note: This memorandum was produced solely by CIA. It was prepared by the Office of Economic Research and was coordinated with the Office of Current Intelligence.

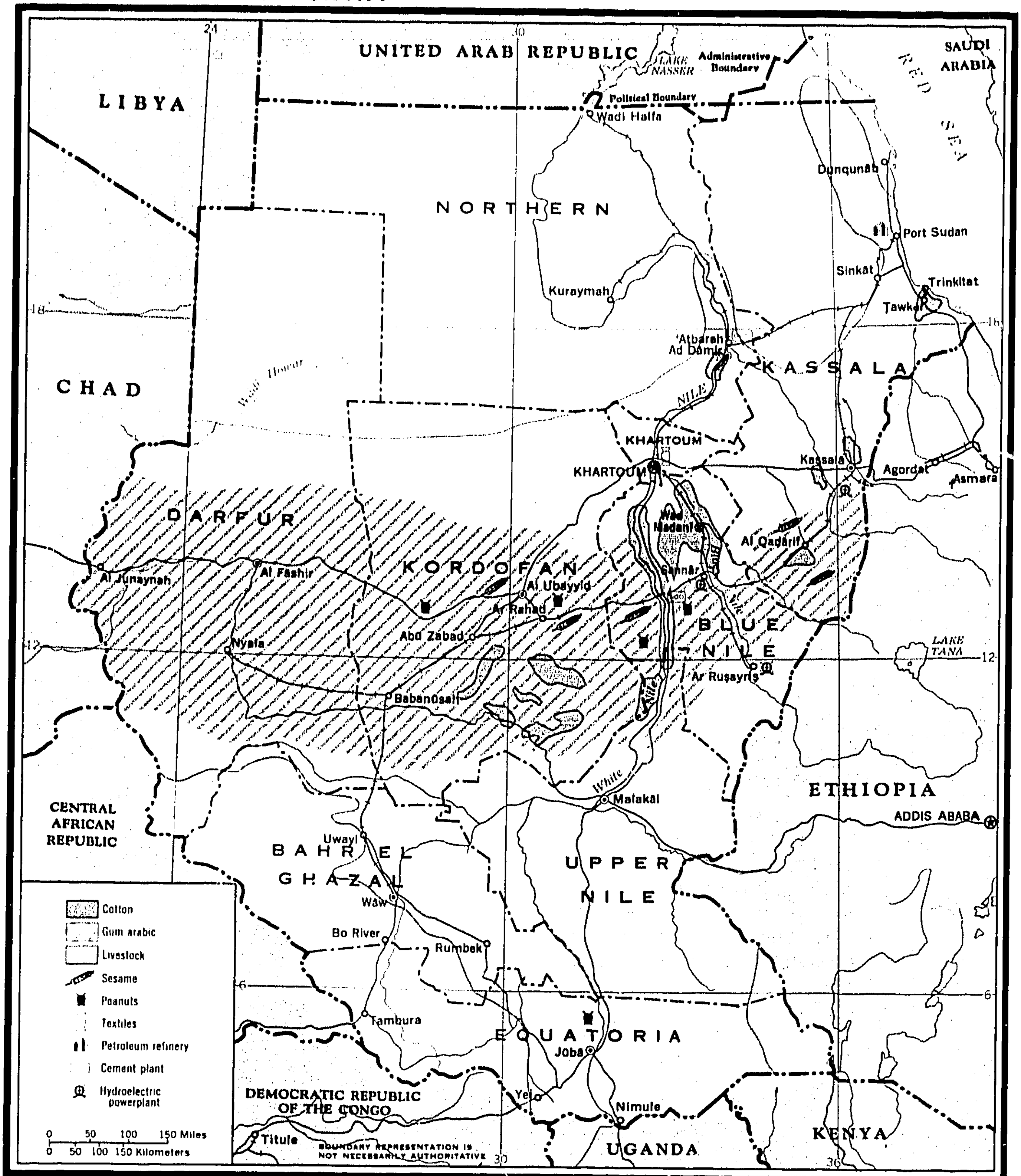
Declassified in Part - Sanitized Copy Approved for Release 2011/10/31 : CIA-RDP85T00875R001600030093-6

by Black Africans and are primarily undeveloped savanna and swamps, where economic activity is restricted almost entirely to nomadic cattle herding and subsistence agriculture (see the map). The Arab north in recent years increasingly has aligned itself with the more radical Arab states; the south, aspiring for freedom from Arab domination, has maintained a now stalemated civil war for the past 15 years.

2. Since the mid-1960s Sudan has been experiencing economic problems caused in part by counterinsurgency costs in the south, but even more by poor development planning and implementation and the unstable political situation. In fiscal year (FY) 1962*, the Sudanese initiated a ten-year development plan, emphasizing expanding agriculture, particularly export crops, and improving transportation. Although the plan goals appeared rather modest, government planning and administration proved inadequate to overcome Sudan's basic weaknesses in productive resources. Outlays for large programs involving irrigation works and railroad improvement were higher than expected, due in part to underestimating the cost of resettling farmers and to speeding up schedules for the railroad program and the Roseires Dam. Moreover, because of the accelerated pace of these major projects, a shortage of skilled labor developed and contributed to operational inefficiencies. Financing became a serious problem in the first four plan years as public investments exceeded plan expectations by $120 million or by 20% (see the chart). The government resorted to the inflationary expedient of domestic bank financing (see Table 1). Foreign exchange reserves were drawn down to finance development imports and to satisfy rising consumer demand generated by government spending. The deteriorating financial position was aggravated in 1964 by a poor cotton crop, which severely curtailed export earnings and accelerated the drain on foreign exchange reserves.

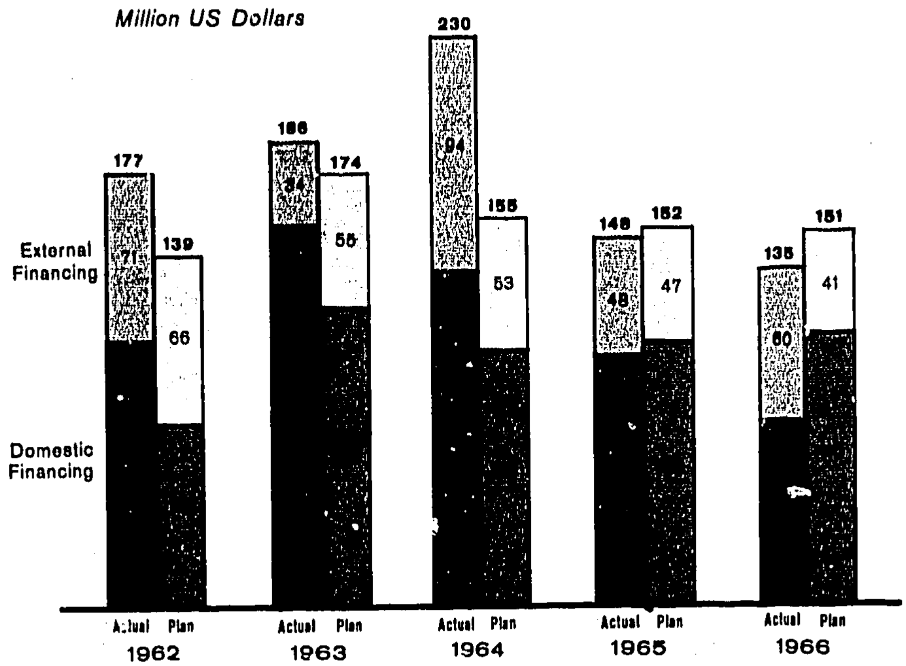
* *The fiscal year of Sudan begins on 1 July of the previous year and ends on 30 June of the stated year.*

SUDAN: ECONOMIC ACTIVITY



78605 7-70

SUDAN: Development Investment, and Financing
First Five Fiscal Years of the Plan



78623 7-70 CIA

25X1

3. In FY 1964 and FY 1965 the drain on foreign exchange reserves reached alarming proportions. Imports in FY 1964 rose to nearly $300 million, an increase of 19%, exports declined by 8% as a result of the poor cotton crop, and the deficit on current account exceeded $100 million (see Table 2). The government reacted by cutting back development expenditures 24% in the following fiscal year and reducing imports some 28%. In spite of a better crop, cotton exports declined still further in FY 1965. Because the Sudanese government set minimum auction prices at a level above world prices, the cotton could not be sold and had to be stockpiled or bartered to Sudan's disadvantage. As a result, a $60 million deficit on current account occurred. Foreign loans and grants helped finance

Table 1

Public Sector Finances a/

Million US $

	Actual						FY 1968		FY 1969		
	FY 1962	FY 1963	FY 1964	FY 1965	FY 1966	FY 1967	Budget	Actual	Budget	Actual	FY 1970 Budget
Central government revenues	173	214	225	203	216	244	261	287	326	329	397
Total public sector expenditures	-228	-257	-325	-305	-317	-318	-370	-344	-369	-417	-490
Central government current expenditures	-148	-168	-174	-173	-213	-241	-246	-257	-296	-330	-391
Development budget expenditures	-69	-105	-121	-92	-92	-72	-132	-83	-77	-84	-92 b/
Net other public activities	-11	16	-30	-40	-12	-5	8	-4	5	-3	-7
Public sector deficit	-55 c/	-44	-100	-102	-102	-74	-109	-57	-43	-88	-93
Deficit financing											
External loans and grants	56 c/	25	45	40	54	43	95	47	37	27	32
Bank financing	20 c/	19	55	61	47	30	13	9	6	61	58
Other	-	-	-	1	1	Negl.	1	2	-	-	3

a. Because of rounding, components may not add to the totals shown.
b. Estimate made prior to the drafting of the development budget which appears in Table 3. Complete revision by sector is not available.
c. The discrepancy between the deficit figure and the necessary financing arises from old bookkeeping methods which, on the one hand, excluded from expenditures certain accruals and advances, while on the other hand treated these items as requiring financing.

Table 2

Balance of Payments a/

Million US $

	Fiscal Years							
	1962 b/	1963 b/	1964	1965	1966	1967	1968	1969
Current account	-80	-46	-105	-60	-53	-50	-53	-44
Trade balance	-48	-1	-68	-27	-17	-26	-28	-16
Exports	195	251	231	189	210	210	227	247
Imports	-243	-252	-299	-216	-227	-236	-255	-263
Net services	-32	-45	-36	-34	-36	-24	-25	-28
Payments	N.A.	-69	-72	-70	-67	-59	-66	-71
Receipts	N.A.	24	36	36	31	35	40	43
Official capital	41	17	31	31	41	30	32	13
Drawings	52	25	45	40	50	41	43	26
Payments	-11	-8	-15	-9	-10	-11	-10	-14
Errors and omissions (including miscellaneous capital movements)	21	21	14	4	-7	-1	6	11
Surplus or deficit	*-18*	*-9*	*-61*	*-25*	*-19*	*-22*	*-14*	*-21*

a. Because of rounding, components may not add to the totals shown.
b. Rough estimates.

these deficits, but foreign exchange holdings fell by some $60 million in FY 1964 and by an additional $25 million in FY 1965.

4. The 1966 budget adopted in December 1965 apparently was designed to win political support for the government rather than to provide a solution for the deteriorating economic situation. In spite of strong inflationary pressures and the effects of continued deficit spending, the budget included increased civil service hiring, wage increases, and tariff reduction -- all expedients that worsened the country's economic problems. With foreign exchange reserves dwindling -- drawn down from $172 million in the early 1960s to about $40 million in the third quarter of 1966 -- and military expenditures on the insurrection in the south increasing, the situation approached crisis proportions.

Efforts at Stabilization

5. In mid-1966 Sudan requested assistance from the International Monetary Fund (IMF). Negotiations resulted in a loan of $28.5 million, and a stabilization program was adopted in September 1966. The program called for increased sales of cotton from stocks held over from the previous year, credit restraint, increased taxation, restraint in recurrent government expenditures, and limitations on bilateral trade agreements and other restrictive trade measures.

6. Progress under the stabilization program was evident as early as the first half of 1967. The annual budget, better attuned to economic realities than those of previous years, included a reduction in public expenditures on development and a reduction in the annual deficit by about 27% from the 1966 level. Moreover, domestic borrowing from the central bank was curtailed to about two-thirds the level of the previous year. Inflationary pressures generated by the policies of preceding years continued, however, and wholesale prices and the cost-of-living index showed their sharpest rises. The closure of the Suez Canal in June 1967 was a major blow to Sudan's efforts to improve its balance of trade as freight rates on European goods increased as much as 75%. Although higher prices for cotton and gum arabic helped to compensate for the higher transportation costs, the

deficit on current account remained at the $50 million level of the previous year. The stabilization program was continued into 1968 when the public sector deficit was further reduced by 23% and domestic bank financing was reduced to less than one-third the 1967 level. In FY 1968 only $9 million was financed by domestic banks in contrast to $61 million in FY 1965, $47 million in FY 1966, and $30 million in FY 1967. Prospects for control of inflationary pressures appeared much improved until mid-1968 when the program was scrapped.

Prelude to a Coup

7. Scrapping the stabilization program at a time when its measures were having a marked effect was due in large part to political instability in the country and the government's inability to pursue the unpopular measures economic austerity required. Bowing to demands by government employees, wage increases ranging from 10% to 27% were granted. A second highly inflationary measure was the honoring of a longstanding commitment to buy private irrigated cotton projects with prompt compensation to the owners and the assumption by the government of the projects' operating losses. A third measure, which was actually a miscalculation, was the takeover of all coffee, tea, and salt trade with the expectation of significant profits. Anticipated profits turned out to be losses, however, which the government had to assume. In a belated attempt to increase revenues, the government increased customs duties, excise license fees, and charges for certain public services. Revenues remained well below expenditures, however, and in FY 1969 the public deficit increased more than 50% above that of the preceding year.

8. With external loans and grants declining, the government sought an unrealistically large IMF standby arrangement (possibly as much as $85 million) but refused to make any concessions on its domestic economic policies. The request was denied, and because of the government's poor showing during negotiations, Sudan suffered a loss in credit worthiness with international institutions and Western countries. To cover the mounting public sector deficit, the government resorted to short-term emergency loans of $19 million from foreign

sources and resumed heavy domestic bank financing, which totaled $61 million by the end of FY 1969.

9. The balance of payments for FY 1969 reflected Sudan's domestic instability and mounting financial crisis (see Table 2). Before the reintroduction of import restrictions, inflation-fed import demand threatened to compromise the effect on the balance of payments of a $20 million increase in exports. Despite the restrictions, imports reached $263 million, more than any other year during the 1960s except FY 1964, thus producing a trade deficit of $16 million. The services account deteriorated somewhat because of larger interest payments on the foreign public debt. The capital account suffered most, however, as capital repayments rose by $4 million while capital inflow dropped by $17 million because of reluctance of foreign countries and international institutions to commit new capital in the Sudan. For the first time, net foreign exchange holdings became negative, hitting a low of -$27 million in December 1968, then recovering only somewhat to about -$15 million at the time of the coup in May 1969.*

The Coup

10. On 25 May 1969, a small group of army officers overthrew Sudan's elected government and installed a ten-man Revolutionary Council and a largely civilian 23-member cabinet to administer the daily affairs of government. Among the several reasons for the coup was disgust with the corruption and public profligacy of previous governments and their failure to solve the country's pressing economic problems. The new government, which includes a number of professed socialists and Communists, is militantly pro-Arab. Two or three of the ten council members and some of the 23 cabinet members are said to be sympathetic to Communist aims. A number of others, including 25X1
Minister of Foreign Affairs and Justice Awadallah, are self-proclaimed socialists closely identified with Egypt, [redacted] 25X1

* *The net negative foreign exchange situation is explained by IMF holdings of approximately $57 million in Sudanese pounds at the end of March 1969.*

Economic Policies of the Revolutionary Government

11. Following the coup, the new government quickly adopted a socialist stance. The regime sought to promote trade relations with the Communist states through bilateral agreements "to avoid the fluctuations of the world market," to broaden the public sector by forming trading monopolies, to draw closer to the Arab states, and to settle the revolt in the south by granting greater autonomy. The regime, however, soon revealed some of the weaknesses of its predecessor. Anxious to gain broad support to secure its power base, it found itself caught between the demands of a deteriorating financial situation and the resistance of its own supporters to the stringent measures required by the economy. Efforts to impose emergency taxes to drain off excess purchasing power were thwarted by widespread public resistance, particularly by the labor unions, and the government apparently did not feel well enough entrenched to enforce this vital measure. Efforts to reduce imports by 50%, another important measure in view of the deteriorating foreign exchange position, encountered resistance in the Khartoum area where the greatest impact was felt. Both prices and unemployment rose as goods became scarce and commercial activity slowed. Government revenues derived from import duties (the traditional source of the major portion of total government revenues) declined, increasing the need for additional bank financing of public expenditures. Inflation continued unchecked; there was an estimated 18% rise in consumer prices between October 1968 and December 1969.

12. The interim development plan for FY 1970, drawn up by the revolutionary government to complete its predecessor's ten-year plan, reflected a more realistic approach to development. The plan stressed completion of those projects already under way that would be uneconomic to abandon, but limited new projects to those from which a quick return could be expected. Priority was given to social service projects in southern Sudan, suggesting a greater awareness of southern problems. The planned budget for the year involved expenditures of $96 million, down $42 million

from the previous year (see Table 3). Allocations, however, were made in approximately the same proportions, and the budget reflected some of the same weaknesses of earlier budgets. In particular, the inflationary practice of financing from domestic, largely bank, borrowing was again resorted to in spite of the serious consequences for the economy -- approximately $25 million or about 25% of total development expenditures was financed domestically. Prices, which had begun to increase rapidly in late 1968, rose even more sharply in the first half of FY 1970, when they increased 8%. While price data beyond December 1969 are not available, it is clear that the rapid rise in prices has continued through June 1970. Planners counted on only $2.9 million from the annual recurrent budget surplus during the year, however, which was a marked improvement in realism over the previous year's expectation of a $28.7 million surplus. Foreign aid donors were to supply approximately $25.6 million, including an International Bank for Research and Development loan of $16.4 million, a Kuwaiti loan of $7.8 million, and a Swedish credit of $1.4 million. Withdrawal in goods from credits was to total $24.7 million, down from $60.1 million in the previous year. The largest withdrawal was $6.6 million of Italian credits and $4.6 million of UK credits. Withdrawals in credits from Communist countries totaled $6.9 million.

13. While pursuing a strong, sometimes vitriolic anti-Western stand, the government has turned to Communist countries in search of trading partners and financial aid. Trade relations have taken the form of bilateral trade agreements with most of the East European Communist countries and the USSR as well as with the United Arab Republic, Japan, and India. An immediate benefit to Sudan's shaky finances was the USSR's agreement to a delay in repayment of past arms deliveries for two additional years (until 1974).* Interest was shown by the USSR in undertaking a series of

* *A $60 million military aid agreement with the USSR was signed in January 1968. Sizable deliveries of equipment began in 1969, but payment was not to begin until 1972.*

Table 3

Interim Development Budget a/

Values in Million US $

	FY 1970	Percent of Total	FY 1969	Percent of Total
Expenditures	96.1	100	137.7	100
Agriculture sector	35.6	37	50.2	36
Industrial mining and public utilities sector	21.2	22	28.1	20
Transportation and communications	18.7	19	27.0	20
Social sciences and public administration	19.2	20	31.0	23
Others	1.4	2	1.4	1
Technical assistance b/	4.0		4.9	
Total revenue	96.1	100	137.7	100
Domestic sources of revenue	46.0	48	44.5	32
Central budget surplus	2.9		28.7	
Surplus from quasi-government corporations	18.1		12.9	
Borrowing from banking system and other local sources	25.0		2.9	

SECRET

SECRET

Table 3

Interim Development Budget a/
(Continued)

Values in Million US $

		FY 1970	Percent of Total	FY 1969	Percent of Total
External sources of revenue		25.6	27	33.0	24
IBRD loan	Roseires Dam	1.4		3.2	
	Sudan railways	4.6		6.6	
	Hydroelectric power	7.2		5.7	
	Educational loan	0.9		1.4	
	Mechanized agriculture	2.3		4.3	
Kuwaiti loan	Sudan railways	0.3		0.9	
	Agriculture	7.5		8.6	
Swedish credit - rural water		1.4		1.7	
British credit - Sudan railways		-		0.6	
Withdrawals in goods from credits		24.7	26	60.1	44
Technical assistance b/		4.0		4.9	

a. Because of rounding, components may not add to the totals shown.
b. Not included in the totals.

development projects and in taking $43 million of Sudanese cotton in a barter agreement. The USSR, because of an opportunity to obtain hard currency for the machinery originally scheduled for Sudan, later postponed fulfillment of its part of the barter arrangement. A number of East European Communist countries promised longer term, low-interest loans for specific projects, but most if not all of these still had not been implemented one year after the coup. The most promising Communist aid offer since the coup, announced in early June 1970, was for credits for equipment and materials for the long-planned Rahad project, a large irrigation project to cost $100 million. It is not clear, however, whether Communist countries will finance the entire undertaking. Among the Arab countries, Libya has responded to Sudanese requests for aid with a $20.8 million cash loan and the promise of additional help.

14. The socialization of the Sudanese economy, threatened even prior to the coup, began in earnest in the last quarter of FY 1970. The first move came in April 1970 when the government announced its intention to exercise an option reserved in a 1962 contract with Shell-BP to purchase 50% (valued at about $2.8 million) of the Shell-BP refinery at Port Sudan. Also in April, the government announced the "Sequestration Act," which gives the Revolutionary Council the authority to sequester (appropriate) the property of any individual, firm, or organization thought to be carrying on activities against the public interest or the economic interests of the state. The right to judicial appeal for relief was denied. On 14 May, President Nimairi announced the uncompensated takeover of holdings of the entire Osman Salih group of companies, one of Sudan's leading firms. The charge leveled at the group was treason and betrayal of the revolution by "cooperation with internal and external enemies of the country." Two days later on 16 May, the government announced nationalization without compensation of the Muhammad Admad Abbas companies, the leading textile firms in Khartoum. Charges were: inordinate profiteering, tax evasion, sale of export licenses, and smuggling currency. Reportedly both seizures severely upset the Sudanese

business community, which previously had thought only foreign firms were threatened.

15. On 25 May 1970, the anniversary of the revolution, a still more extensive series of take-overs was begun. The government announced the nationalization of the entire banking sector and of four British trading companies and terminated the licenses of foreign insurance firms. The nationalized banks included British, American, Ethiopian, United Arab Republic, French, Jordanian, and private Sudanese interests. Only nine days later, President Nimairi announced the "sequestration" of 16 companies and commercial organizations and the nationalization of one Egyptian-owned cement plant. Three of the companies were wholly Sudanese owned, and the rest were owned by foreigners (Greek, Syrian, Armenian, Lebanese), many of whom were citizens of Sudan. Charges leveled against "sequestered" companies included financial, administrative, and trade control manipulation; aiding Zionists; and the fact that large estates were "acquired by corrupt Capitalist means." Less than two weeks later, on 14 June, ten more firms were nationalized and the assets of 23 businessmen were confiscated. At the same time, the government established monopoly control of all cotton marketing and of the import and distribution of all commercial movie films. Among the firms nationalized were the BATA shoe factory (Canadian), the Blue Nile Brewery (British), and a number of US-owned service and distribution agencies including National Cash Register and several rubber companies. The only significant difference between "nationalization" and "sequestration" apparent in these moves is that nationalization envisions some type of compensation, usually in the form of 15 to 25 year bonds, while owners of sequestered firms appear to receive no compensation, although some may continue to receive salaries.

Prospects and Conclusions

16. The difficult economic situation faced by the present Sudanese government developed over the past decade and stems in part from poorly managed and overzealous development efforts. Inefficient, weak, and often corrupt governments, frequently rent with internal dissension, were unable to carry out the rigorous measures required to restrain inflation while encouraging development. Officials drew heavily on foreign exchange and borrowed extensively from the banking system to finance development expenditures and rising imports. The resulting persistent inflationary and balance-of-payments problems reached a climax in FY 1969 when foreign exchange holdings became negative.

17. The revolutionary government installed by the May 1969 coup has adopted measures to build a "fully socialist structure based on workers." The nationalization and expropriation of financial and commercial concerns and assumption of governmental control over economic activities apparently has exceeded even the expectations of the Sudanese Communist Party. These actions have had a major effect in deterring foreign and domestic investment. An anti-Western stand has been taken, and the USSR, Eastern Europe, and certain Arab countries have been approached for assistance. To maintain a flow of essential goods despite the acute shortage of foreign exchange, the government has resorted to bilateral trade agreements, chiefly with the USSR and the East European Communist countries.

18. Rebellion in the south still smoulders, causing a small but persistent drain on the national budget, and the uprising of the ANSAR, a Moslem religious sect, in March and April 1970 caused a severe strain on finances as defense expenditures increased. Communist aid at best has alleviated only a few pressures, and bilateral trade agreements have proved to be no panacea for the nation's financial ills. All too often the goods obtained under these agreements are not the best choice for the economy's needs, and over-reliance on barter arrangements has curtailed the amount of foreign exchange available for debt servicing and other payments abroad. On the other

hand, cotton production and sales are progressing well. The major purchasers during the first quarter of 1970 were the USSR and, to a lesser extent, India and West Germany.

19. Until June 1970, when the USSR, Czechoslovakia, and other Communist countries offered credits for the Rahad project, Communist aid had been disappointing. Although too early to be certain, should this offer prove to be the forerunner of equally generous offers, development prospects would improve greatly. During the 1960s, however, only $17 million of Communist aid was disbursed out of $123 million extended. Communist aid will have to be large, moreover, to compensate for declining Western aid, which virtually will cease when present commitments are fulfilled. To return to an accommodation with major Western aid donors, currently used as scapegoats for many of Sudan's problems, would require a sharp and unlikely reversal of the country's political stance.

20. The "sequestration" and nationalization of firms and businesses is a relatively new element to consider in Sudan's uncertain economic future. The full confiscation of personal belongings, unannounced searches, refusal to allow salaried managers of firms to leave the country, and prison or house arrest of businessmen attest to the military rulers' depth of suspicion toward the commercial community. These actions doubtless will result in some chaotic months in Sudanese economic affairs before a new balance is restored. Reportedly, private business confidence has been destroyed completely, and further private investment, both foreign and domestic, is unlikely. The country's economic future will depend increasingly on the regime's ability to provide the economic planning and direction required in a socialist state. Failure could result in sharply curtailed economic activity or at best in gradual deterioration of the economy. During its first year in power the government was not well enough entrenched to impose the stringent measures required to bring inflationary pressures under control, but the recent adoption of police state powers may make such measures possible.